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Supreme Court, U.S.
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No. 02-1135

IN THE

Supreme Court of the United States

ALABAMA INSURANCE GUARANTY ASSOCIATION, ET AL.,

Petitioners,

v.

UNITED STATES AND JOHN ASHCROFT, IN HIS OFFICIAL CAPACITY AS ATTORNEY GENERAL OF THE UNITED STATES,

Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

PETITIONERS' REPLY BRIEF

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STATEMENT PURSUANT TO RULE 29.6

Pursuant to Supreme Court Rule 29.6, the Petitioners incorporate the corporate disclosure statement made in the Petition for Writ of Certiorari and state that it is current.

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PETITIONERS' REPLY BRIEF

Pursuant to Supreme Court Rule 15.6, the Guaranty Funds submit this reply to address new arguments made in the Brief for the Respondents in Opposition ("U.S. Opp. at ___.").

I. *UNITED STATES V. SUMMERLIN* DOES NOT APPLY BECAUSE CONGRESS HAS CEDED AUTHORITY TO THE STATES FOR THE REGULATION OF THE BUSINESS OF INSURANCE.

The United States contends that *United States v. Summerlin*, 310 U.S. 414 (1940), should be the beginning and the end of the inquiry as to whether the state time bar applies to the United States. *Summerlin* held that the United States is not bound by state statutes of limitations unless Congress provides otherwise. *Id.* at 416. The United States further contends that *Summerlin* is outside the scope of McCarran-Ferguson because McCarran-Ferguson states that "no act of Congress" shall be construed to preempt a state law "regulating the business" of insurance. The United States reasons that because the principle espoused in *Summerlin* is not an "Act of Congress," McCarran-Ferguson has no bearing, and *Summerlin* therefore applies. The United States puts the cart before the horse.

If the Court were to approach the issue as the United States proposes, the Court would be substituting federal common law for subsequent explicit legislation of Congress. The federal common law principle that the United States is not subject to state statutes of limitations is a general principle that preceded the McCarran-Ferguson Act. As the United States notes in its opposition, the McCarran-Ferguson Act was a specific act by Congress in reaction to the Court's decision in *United States v. South-Eastern*

Underwriters Ass'n, 322 U.S. 533 (1944). U.S. Opp. at p. 4. Congress carved out the specific field of the "business of insurance" for regulation by the states. For any federal law to regulate the business of insurance, such law must specifically relate to the business of insurance. 15 U.S.C. § 1012 (stating that no federal act shall preempt a state law of insurance, "unless such Act specifically relates to the business of insurance"). To the extent that any pre-existing general law, such as the *Summerlin* principle, may have affected the "business of insurance," McCarran-Ferguson changed the scheme.

Adopting the United States' interpretation of the McCarran-Ferguson Act would defeat the Act's very purpose to cede the regulation of insurance to the states. The United States' interpretation would allow federal common law, rather than state law, to regulate the business of insurance. The fact that *Summerlin* is not "an Act of Congress" is irrelevant.

Instead, the Court must look to the McCarran-Ferguson Act and determine whether the state time bar "regulates the business of insurance." If it does, then the time bar falls clearly within the scope of McCarran-Ferguson. It is only if the Court determines that the time bar is not a law regulating the business of insurance that *Summerlin* would play any role in this case.

II. THE UNITED STATES MISREADS AND FAILS TO APPLY THE PRINCIPLES SET FORTH IN *FABE*.

In its preliminary discussion of the case, the United States describes *United States Dep't of Treasury v. Fabe*, 508 U.S. 491, 509 (1993), as holding that certain state provisions "'regulated the business of insurance' because they were aimed at the insurer-insured relationship, i.e., ensuring that the insurer would fulfill its promises." U.S. Opp. at p. 7. Indeed, the time bar is aimed at the insurer-insured

relationship because, without it, no receiver will make distributions to policyholders for fear of being held liable for subsequently filed claims of the United States. Thus, no policyholders will be paid in breach of the promise made by the insurer. The United States, however, never addresses the relationship between the time bar date and the insurer-insured relationship. Instead, the United States seizes upon the Court of Appeals' twice misapplied reading of *Fabe*.

In *Garcia v. Island Program Designer, Inc.*, 4 F.3d 57 (1st Cir. 1993), and now in *Ruthardt*, the Court of Appeals interpreted *Fabe* to preclude reverse preemption of the state time bar on the basis that the time bar benefited policyholders and general creditors to the same or similar degree. As demonstrated by the uncontradicted factual record, however, the time bar has a substantially greater effect on policyholders than on general creditors because policyholders are given priority over other creditors. Moreover, given the limited amount of assets available for distribution in this estate, the policyholders are the only persons who will be paid and thus are the only persons benefited by the time bar. A similar effect is present in most estates inasmuch as estate assets are limited and policyholders tend to receive greater recoveries than general creditors. Pet. App. 73a, at ¶ 27.

Not only did the Court of Appeals misapprehend the extent of the time bar's impact on policyholders, it misread *Fabe*. The concomitant benefit to general creditors and policyholders does not preclude reverse preemption *provided the statute is reasonably necessary to further the goal of protecting policyholders*. *Fabe*, 508 U.S. at 509. Just like the Court of Appeals, the United States failed to apply this standard. Enforcement of a time bar is more than reasonably necessary to further the goal of protecting policyholders and ensure that the promise of the insurer is upheld. The time bar is just as necessary to

protect policyholders as the administrative expense priority upheld in *Fabe*. An incidental benefit to general creditors did not preclude McCarran-Ferguson protection for the administrative expense priority upheld in *Fabe*. An incidental benefit to general creditors from the time bar should not preclude McCarran-Ferguson protection for the time bar.

III. THE DECISION OF THE COURT OF APPEALS HAS THE PRACTICAL EFFECT OF PREVENTING THE RECEIVER FROM PAYING POLICYHOLDER CLAIMS.

At page 17 of its opposition, the United States makes the remarkable proposition that the Receiver can somehow make payments on timely policyholder claims despite outstanding claims of the United States for which the Receiver has no notice. U.S. Opp. at p. 17 ("And the decision in this case nowhere declares that States cannot pay timely policyholder claims ahead of untimely policyholder claims for which they have no notice (including those of the United States)"). Such position has never before been expressed by the United States in the context of the American Mutual liquidation. Indeed, this comment underscores the misapprehension by the courts and the United States of the reality that no Receiver in any liquidation, for fear of personal liability, will make distributions without assurance that all federal claims have been made or otherwise waived. No such assurance or waiver has been provided here nor in many other similar liquidation proceedings. Receivers, policyholders, and guaranty funds now need the Court to determine whether the United States may hold this key to the completion of insurer liquidation proceedings nationwide.

IV. THERE IS NO JURISDICTIONAL BARRIER TO FURTHER REVIEW BY THE COURT.

As its final argument in opposition to the petitions, the United States raises the issue of jurisdiction as one "not yet addressed by the parties or the courts." U.S. Opp. at p. 18. To the contrary, jurisdiction was addressed by the Receiver in her Complaint, therefore warranting no further attention from the parties, the District Court, or the Court of Appeals - until now, as the United States seeks to avoid the Court's final review of the time bar issue.

In her Complaint, the Receiver alleged federal question jurisdiction under 28 U.S.C. § 1331, given the material questions arising under two federal statutes - the McCarran Ferguson Act, 15 U.S.C. § 1012, and the Federal Priority Act, 31 U.S.C. § 3713. Complaint, ¶ 2. Also in her Complaint, the Receiver addressed sovereign immunity by asserting that the action is one for "non-monetary specific relief concerning a federal agency's final action or failure to act which have substantially impaired the Receiver's ability to discharge her obligations under Massachusetts law," thus falling within the waiver provided under the Administrative Procedures Act ("APA"), 5 U.S.C. § 702. Complaint, ¶ 2. In the alternative, the Receiver asserted that the action is one falling within the *ultra vires* exception under *Larson v. Domestic & Foreign Commerce Corp.*, 337 U.S. 682, 689-90 (1949), because the Attorney General has acted beyond the scope of his statutory authority. The Receiver was correct on both grounds.

A. The action was properly brought under the Administrative Procedures Act.

The United States challenges jurisdiction under the APA, contending that the Receiver has not sought to challenge final agency action nor to compel agency action that has been withheld. Such a position,

however, is contrary to the face of the Complaint and to the consistent treatment of the dispute by both the parties and the courts. In her Complaint, the Receiver alleges that:

> The United States, acting by and through the Department of Justice and defendant Attorney General Reno, has asserted that all federal claims are entitled to a first priority under 31 U.S.C. § 3713, notwithstanding the priorities for distribution or time limits for claims established by state law.

Complaint, ¶16. The Receiver further alleges that "[t]he United States has taken the position that claims by it are not subject to time limits imposed by state law for claims against the estates of insolvent insurers." *Id.* at ¶ 17.[1]

It is the stated final position of the United States, as expressed through the Attorney General, that the United States is not subject to state insurer insolvency bar dates. That stated position is the final agency action from which relief is sought. Indeed, such position has resulted in the indefinitely stalled insolvency proceedings of AMLICO and AMI, like so many other insurer insolvency proceedings nationwide, causing substantial injury to the Receiver, policyholders, and guaranty funds. As alleged:

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[1] Count III of the Receiver's Complaint sought an order, pursuant to 5 U.S.C. § 706, that the United States act upon the Receiver's request for assent or conditional waiver to a fifth distribution. During the course of the litigation, the United States denied the Receiver's request, and the District Court therefore found Count III to be moot. *See* Pet. App. 49a, n.30. The United States' contentions that the claim for relief from the United States' failure to act was abandoned and never addressed by any court are without merit. U.S. Opp. at p. 20.

> [i]f the Receiver distributes assets upon approval of the Supervisory Court, and the position of the United States later prevails, the Receiver faces potential personal liability under 31 U.S.C. § 3713 (b). Thus the position of the United States prevents her from performing her duties to complete the liquidation of the Companies under state law.

Complaint, ¶ 21.

The position of the United States and comments of the courts below reflect the Receiver's proper construction of the Complaint as seeking relief from final agency action. *See, e.g.,* Complaint, Exhibit B (United States Department of Justice asserting "priority status" on behalf of "the United States its departments, agencies and instrumentalities" and stating "[t]o the extent Massachusetts law is inconsistent with federal law in this regard, *it is inapplicable*") (emphasis added); Pet. App. 4a (First Circuit Court of Appeals stating that "[t]he United States has asserted throughout that . . . the one-year bar date does not apply to any of its claims"). Thus, the action properly falls within the scope of the APA. The action seeks judicial review of and non-monetary specific relief from the final position of the United States, as expressed by the Attorney General, which position continues to adversely affect the Receiver, policyholders, and guaranty funds. *See Lujan v. Defenders of Wildlife*, 497 U.S. 871, 882 (1990) (holding that plaintiff may be entitled to judicial review under § 702 if the complaint properly identifies agency action that affects plaintiff in a specified fashion).

B. In the alternative, the action was properly brought under *Larson v. Domestic & Foreign Commerce Corp.* because the Attorney General has acted outside of his statutory authority.

Under *Larson v. Domestic & Foreign Commerce Corp.*, an action may be brought against a federal officer for specific relief when either (1) the officer is acting beyond the scope of his statutory authority or (2) the statute conferring such authority is claimed to be unconstitutional. 337 U.S. 682, 689-90. The current action falls within the first category of cases in which the federal officer is alleged to have acted outside the scope of his authority. In such cases, the officer is not acting as the sovereign, the sovereign therefore is not being sued, and accordingly no waiver of sovereign immunity is required.

In this case, the Attorney General is acting outside the scope of his authority by asserting claims that conflict with the statutory constraints explicitly imposed by Congress in the McCarran-Ferguson Act. McCarran-Ferguson carved out the business of insurance for regulation by the states. By asserting that the state time bar must yield to the Federal Priority Act, the Attorney General violates state law and McCarran-Ferguson. McCarran-Ferguson limits the authority of the Attorney General in areas where the states have regulated the business of insurance. Here, the Attorney General has sought to exercise his authority despite reverse preemption explicitly dictated by Congress, therefore acting *ultra vires* to his authority.

The United States attempts to liken the current action to the circumstances in *Larson* which led the Court to conclude that an action should not lie against the federal officer, i.e. the Court's finding that the action sought to dispose of the sovereign's property and therefore was a suit against the

sovereign. U.S. Opp. at p. 21. Here, however, the action does not seek to deprive the United States of property. Instead, the action seeks to determine the interplay between federal and state laws in light of the reverse preemptive scheme established by McCarran-Ferguson, ultimately determining how a federal claim against an insolvent insurer should be brought, not whether such a claim may be brought.

The fact that a decision in favor of the Receiver may result in the United States being unable to assert certain claims is not determinative. In the event the Court finds the United States is subject to the time bar, the unasserted claims of the United States will have been lost by the United States' failure to act and would not be viable property interests to begin with. The facts in *Larson* have no bearing on the outcome here. Rather the legal principles in *Larson* provide an alternative basis for the current suit against the Attorney General of the United States.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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